



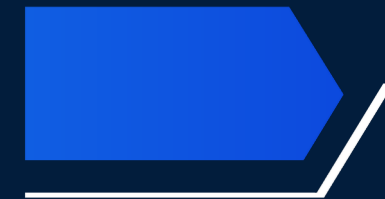
BASIC OVERVIEW OF INDIAN TRANSFER PRICING

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INTERNATIONAL TAX

Table Of Content



BACKGROUND



MEANING



EFFECTS



CASE STUDY



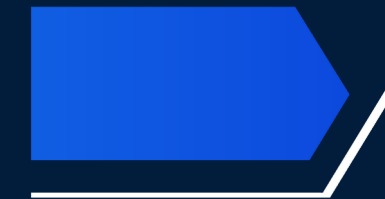
SECTION 92A-F



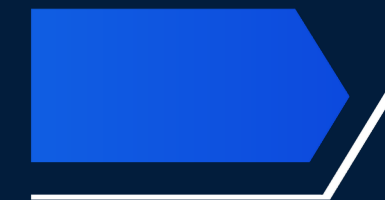
ECONOMIC ANALYSIS



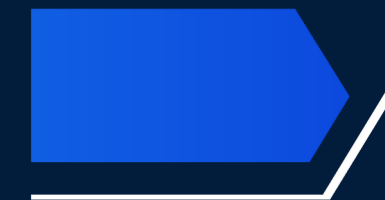
DOCUMENTATION & OECD ACTION PLAN



TAX AUDIT PROCEDURE



SAFE HARBOUR RULES



ADVANCE PRICING AGREEMENT



APA PROCESS



PENALTIES



BACKGROUND

INTRODUCTION OF FDI AND
INTREST FROM MNCs

1990

1991

STANDING COMMITTEE SET UP
FOR DISCUSSIONS ON TP

CBDT EXPERTS RECOMMENDED
OVERHAUL OF THE OLDER TP
PROVISIONS

1999

2001

INTRODUCTION OF INDIAN
TRANSFER PRICING
REGULATIONS (TPR)

AMENDMENTS TO BRING IN
LINE WITH OECD GUIDLINES
ON TP

2002

WHAT IS TRANSFER PRICING?

Prices that one division in a company charges another division for goods and services provided especially when one such division is from another tax nation

TPR help in keeping a check on possible tax leakages in cross border intra-group transactions.

In short, by charging above or below the market price, companies can use transfer pricing to transfer profits and costs to other divisions internally to reduce their tax burden.

EFFECTS OF TRANSFER PRICING

The effect is such that parent company or a specific subsidiary tends to produce insufficient taxable income or excessive loss on a transaction within the group.

Transfer pricing acts to distribute earnings throughout an organization but is primarily used to skirt tax laws and reduce tax burdens by multinational companies.

Transfer pricing provisions are governed by section 92A-F of the Income Tax Act and Rule 10A-E of the Income Tax Rules, 1962.

EXAMPLE



- Entity A sells at higher value to Entity B
- Costs for Entity B in higher tax jurisdiction (India) are shown higher, triggering the profits to decrease, in the end leading to the taxable profits to reduce and tax savings of the MNC as a whole.

IMPORTANT SECTIONS

92A

ASSOCIATED ENTERPRISES

One of them participates in the management, control, or capital of another;

There is common management, control, or capital exercised by some persons.

92B

INTERNATIONAL TRANSACTIONS

Transaction between two or more associated enterprises (AEs) and either or both of them are non-residents.

92C

COMPUTATION OF ALP

A price that is applied to transactions between persons other than AEs in uncontrolled conditions.

IMPORTANT SECTIONS

92D

DOCUMENTATION

Rule 10B lists the documents to be maintained.

92E

ACCOUNTANT'S REPORT

Audit report with all the details and the form 3CEB shall be filed

92F

OTHER DEFINITIONS

This section contains certain definitions relevant to computation of arm's-length price

ECONOMIC ANALYSIS

A. SELECTION OF TESTED PARTY

When the tested party is a foreign AE, the foreign comparables are used for benchmarking

There is no specific prohibition in the TP Regulations regarding use of foreign comparables.

The difference in Indian GAAP vis-à-vis accounting principles and practices of other countries are usually major reason why tax authorities reject foreign comparables

Tax authorities have held that if a taxpayer wishes to consider a foreign AE as the tested party, then relevant data for comparison should be available in the public domain or should be furnished to the tax administration

ECONOMIC ANALYSIS

B. METHODS OF ALP COMPUTATION

Comparable
Uncontrolled Price
(‘CUP’) method

Resale Price
Method or Resale
Minus Method
(‘RPM’)

Transactional net
margin method
(TNMM)

Cost Plus Method
(‘CPM’)

Profit Split
Method (‘PSM’)

ECONOMIC ANALYSIS

C. SELECTION OF PROFIT LEVEL INDICATOR (PLI)

Selection of appropriately PLI depends on:

Nature of the activities of the tested party

The reliability of the available data with respect to comparable uncontrolled taxpayers

The extent to which a particular profit level indicator is likely to produce a reasonable determination of the income that the tested party would have earned had it dealt with the controlled taxpayer at arm's length

Economic Analysis

PLI	REMARKS
Gross Profit/ Sales	Appropriate for trading activity
Net Profit/ Operating Costs	Appropriate for indenting activity
Net Profit/ Operating Assets	Appropriate for capital intensive industry
Cash Profit Ratio	New Business with Heavy Investment
Return on Capital Employed	Capital Intensive Business
Return on Shareholder's Funds	Highly Geared Companies
Revenue per Employee	Human Capital Based Based

ECONOMIC ANALYSIS

C. Search Process

Step 1. Identification of companies engaged in activities that are potentially comparable to the activities of tested party

Step 2. Quantitative analysis – application of filters : –Data availability filter –Turnover filter –Net worth filter –Trading / Manufacturing / Service Income to total Income filter –Related party transaction filter

Step 3. Qualitative analysis - analysis of the information contained in the databases and/or annual reports

Step 4. Final validation of the potential comparable companies through additional research and a close scrutiny

ECONOMIC ANALYSIS

C. Search Process

Step 5. Selecection of PLI

Step 6: Margin of the comparable – range/weighted average

Step 7: Margin of Comparable v/s tested party

AO refers case to TPO with prior approval from IT Commissioner if value of transaction >50 million INR

TPO sends notice to taxpayer for more evidence to support the claim of ALP

Reply within 30 days and in some case maximum upto 60 days

Scrutiny assessment takes place with maximum upper limit of 36 months to 48 months

Order passed by TPO and copy sent to AO for computation of taxable income

Order passed by AO and scrutiny assessment reaches completion

TAX AUDIT PROCEDURE

A fixed amount of tax returns are selected on the detailed audit.

6 months notice period is sent from the financial year end in which returns were filed

DOCUMENTATION

The provision in Section 92D contained in the TPR are exhaustive as far as maintenance of documentation is concerned

Back ground information like nature of transaction, analysis carried out to select the most appropriate method and to identify comparable transaction and the actual working out of the ALP and whether they are calculated as per the TPR

This includes report of an accountant certifying that the ALP has been determined in accordance with TPR

DOCUMENTATION

The prescribed documentation shall be maintained and retained for 8 years

The primary responsibility is on the taxpayer to determine an ALP in accordance with the TPR and to substantiate the same with the prescribed documentation.

The details shall include a detailed description of the ownership, profile of the MNC,

SECTION 92D read with RULE 10D

10D(1)(a)

Description of ownership
structure

10D(1)(h)

Record of analysis for finding
comparability

10D(1)(b)

Profile of MNC- name,address,tax
country of all AE

10D(1)(i)

Description of method considered
for computation of ALP

10D(1)(c)

Business description

10D(1)(j)

Record of analysis for finding
comparability

10D(1)(d)

Terms of international
transactions

10D(1)(k)

Assumptions and policies which
affected determination of ALP

10D(1)(e)

FAR analysis description

10D(1)(l)

Details of adjustments relevant
for computation of ALP

10D(1)(g)

Record of uncontrolled
transactions and comparables

10D(1)(m)

Any other information relevant
for ALP

Robust and detailed
FAR and Economic
Analysis

Transfer pricing
assessment
experience

BEST TP DOCUMENTATION PRACTISE

Comprehensive and
detailed

Cognizance of
Indian & overseas
judicial rulings

Application of OECD
principles and
guidelines

Consistent with
Master File

OECD BEPS ACTION PLAN

India has introduced the concept of three tier TP documentation in the year 2016 to be in line with the OECD guidelines. An entity which is part of a multinational enterprise (MNE) group is required to maintain the following group information by way of three files:

Local File (Section 92D)

Master File- Form 3CEAA

Country by country reporting
(CBCR)- Form 3CEAA

Emphasised in BEPS Action Plan 13 wherein the constituent entities are required to maintain a Master plan and Country-by-Country Report as per transfer pricing provisions Form 3CEAA.

PART A OF FORM 3CEAA	PART B OF FORM 3CEAA
Basic information like the name of the international group, entities involved in that group, their details like PAN and permanent address, etc. It shall be filed by every entity that has entered into any international transaction, irrespective of any limits or threshold of the value.	Part B of the Form 3CEAA does not apply to everyone. It is to provide in-depth details Has to filed if 2 conditions are followed: 1.Consolidated group revenue for PFY exceeds Rs. 500 crore 2. Total value of the international transactions has exceeded Rs. 50 crore and Rs. 10 crore if transaction involves Intangible property.

MASTER FILE

Country-by-Country Report (CbCR) is required to be electronically filed in India where

- 1.The Ultimate Parent Entity (UPE) of the Multinational group (MNE) is resident in India or
- 2.Where the MNE has designated an alternate reporting entity for the purposes of filing CbCR in India.

ELIGIBILITY	DUE DATE AND FORM
Where the annual consolidated group revenue as per the consolidated financial statements of the MNE group in the immediately preceding accounting year relevant to the Indian financial year, is more than INR 64 billion.	The due date for filing CbCR is in the prescribed Form no. 3CEAD in India is 12 months from the end of reporting accounting year of the UPE preparing consolidated financial statements.

CbCR

The circumstances in which the income-tax authorities shall accept the transfer price declared by the assessee. It substitutes simpler obligations for those under the general TP regime.

For those who are engaged in

1. ~~Providing information technology development services or KPO services, etc with insignificant risk, to a non-resident associated enterprises.~~
Providing information technology development services or KPO services, etc with insignificant risk, to a non-resident associated enterprises.
2. Intra group loan, corporate guarantee, providing contract research and development services wholly or partly relating to software development, etc with insignificant risk, to a foreign principal.

SAFE HARBOUR RULES

Advance Pricing Agreement

Transfer prices are negotiated in advance with the tax authorities

APA filing fees w.r.t value of transactions

Unilateral, bilateral or multilateral

<INR 100 Crores = INR 10 lakhs

For any tax payer with an international transaction

>INR 100 crores but < INR 200 crore = INR 15 lakhs

Validity upto 5 years

>INR 200 crores
= INR 20 lakhs



APA PROCESS

PENALTIES

Sections	Nature of Penalties	Quantum of Penalty
Section 270A	Penalty of under-reporting of income as a consequence of failure to report international transactions,	50% of the amount of tax payable in case of underreporting and a penalty of 200% of the amount of tax payable in case of misreporting
Section 271AA	Penalty for failure to maintain documents, report a transaction, or maintaining or furnishing incorrect information under Section 92D	2% of the value of international transaction
Section 271G	Penalty for failure to furnish documentation prescribed under Section 92D(3) of the Act	2% of the value of international transaction
Section 271BA	Penalty for failure to furnish Accountant's Report in Form 3CEB as required under Section 92E	1,00,000 INR

Thank You

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